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Overview of Contractual Risk Transfer

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INTRODUCTION

1. Contractual Risk Transfer Strategies
2. Basics of Construction Contracts
3. Questions and Answers



POLL QUESTION:

Do you review and/or write contracts as part of your job duties?



Yes



No

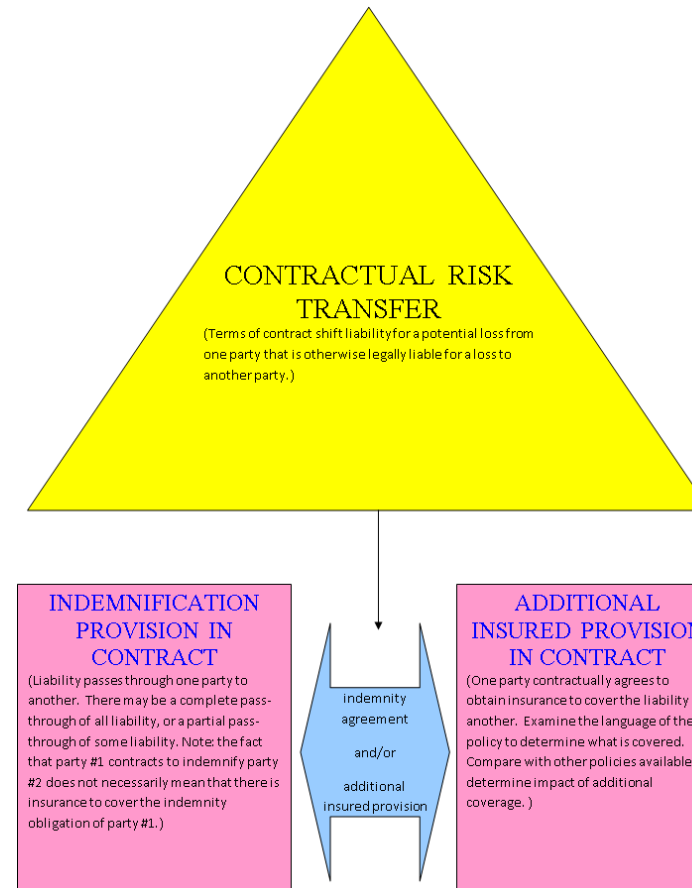


OVERVIEW OF CONTRACTUAL RISK TRANSFER STRATEGIES

- Your Goal: accept what you can finance, transfer the rest
- Indemnity Clause is the most obvious means of transfer but it's not the only



Risk transfer through contract and insurance provisions



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CONTRACT REVIEW PROVISIONS

- Contracts govern and regulate the relationships among numerous parties on a job site
- Do not sign a contract without reviewing the terms and conditions
- Request any changes, additions, or deletions prior to execution



INTERPRETATION OF CONTRACTS

- In order to avoid judicial intervention, contracts must be clear and unambiguous
- Courts will not rewrite the contracts, but will try to ascertain the intent of the parties at the time contract was signed, not at time of breach
- Words and other conduct are interpreted in light of all circumstances
- Interpretation against the party drafting the contract





RISK TRANSFER THROUGH CONTRACT

Types of businesses that might use contractual risk transfer: **ANY and ALL!**

- Most commonly involved in construction, real estate and property loss scenarios
- In real estate scenarios
- It may exist between landlord and tenant or;
- Property owner and property manager
- As well as property owner and service providers (i.e. Janitorial)
- Any relationship where one party wants another to be financially and legally responsible for a loss.



Overview of Contractual Risk Transfer Strategies

Overview of Contractual Risk Transfer

- Indemnity Provisions
- Three Types of Indemnity
- **Broad Form:** Party assuming liability is responsible for all negligence, even the sole negligence of other party
- **Intermediate Form:** Party assuming liability is responsible for all but the sole negligence of the other party
- **Limited Form: Each party is responsible for its own portion of fault; this is the only clause that is valid in Colorado construction projects**
- Anti-Indemnity Statutes
- State laws that restrict what types of negligence may be assumed by a party to a contract

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RISK TRANSFER THROUGH CONTRACT

- We have all seen language like, "hold harmless, indemnify and defend."
- These words inure to the benefit of the **indemnitee, the entity which is to be indemnified. The indemnitor is the party that assumes the proscribed risk.**
- Oftentimes, the status of indemnitee or indemnitor factors into the cost of a policy given the risks that may be transferred.
- When the indemnitee (or its counsel) tenders to the indemnitor under the contract provisions, it is asking the indemnitor to assume all legal and financial responsibility for the claim. This may mean litigating the case by defending the indemnitee, paying for legal fees, or paying any settlement or verdict. The parameters are dictated by the contract. Thus, it is important from the beginning of the contractual relationship to include language that may one day become necessary to litigate.



POLL QUESTION:

Would you rather be an indemnitee or an indemnitor?



Indemnitee



Indemnitor



HOW TO BUILD YOUR INDEMNIFICATION LANGUAGE

Sometimes, “any and all” doesn’t mean “any and all”

- The decisions of the Court in each jurisdiction are important inasmuch as they outline what language requirements the Court requires to uphold contractual clauses.
- Risk can be transferred from one party to another by means of the appropriate language in the contract.



DIFFERENT TRIGGERS IN ENDORSEMENTS

- Liability arising out of “your work.”
- Liability arising out of “your ongoing operations performed for that insured.”
- Liability arising out of “the negligence of the named insured.”

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Example of contractual indemnification scenario and sample language

For example, general contractor ACME hires as a subcontractor Shoddy Destruction Co. The subcontract agreement includes an indemnity agreement calling for Shoddy Destruction Co. to indemnify ACME in the event that there is an accident or injury on the work site for which ACME is legally responsible.

After construction is underway, an employee of Shoddy Destruction Co. is injured in a work-related accident at the construction site. The employee sues the general contractor ACME, alleging that ACME's negligence caused his accident and resulting injuries. ACME may be able to enforce the indemnity agreement it has with Shoddy Destruction Co. and thereby require Shoddy Destruction Co. to indemnify or reimburse ACME for any damages ACME owes to the employee as a result of the accident.



Example of contractual indemnification scenario and sample language (cont.)

Keep in mind that, generally, when an employee is injured while working, that employee is entitled to receive the benefit of workers' compensation insurance obtained by his or her employer. The workers' compensation benefits typically cover the injured employee's medical expenses and lost wages as required by law. The workers' compensation benefits are paid regardless of whether the employer was negligent or otherwise caused or contributed to the employee's injury.

The employee usually gives up his or her right to sue their employer in exchange for receiving the right to receive workers' compensation benefits. However, the employee does not give up the right to sue parties other than their employer to recover damages resulting from the injury.





POLL QUESTION:

What benefits is Shoddy responsible for?

a. None

b. Workers' Compensation Benefits

c. Damages resulting from negligence including bodily injury and pain and suffering

d. Both B and C

Example of indemnification scenario and sample language (cont.)

Thus, in the example, the fact that the hypothetical employee is entitled to receive the benefits of workers' compensation insurance paid for by Shoddy Destruction Co. does not preclude the employee from bringing a liability action against ACME. Moreover, the fact that Shoddy Destruction Co. has workers' compensation insurance that covers the employee's medical expenses and lost wages would not preclude ACME from enforcing the indemnity agreement.

In other words, under these circumstances, Shoddy Destruction Co. could be liable for both workers' compensation benefits owed to the employee as well as negligence liability damages, including damages for pain and suffering.





Additional insured issues

Does the trade contract require an individual entity to be named as an additional insured on a general liability policy of insurance?

The contract should clearly state the intentions of the parties as to whose insurance will apply as primary insurance.

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Certificates of Insurance

CERTIFICATES OF INSURANCE

Certificates of Insurance may identify a particular party as a “certificate holder or an additional insured.” Generally, a Certificate of Insurance is not evidence of insurance. However, because this is an issue that varies by jurisdiction, a review of how the jurisdiction involved treats this question should be done.

It is important to check the policy language and in particular the additional insured endorsement issued by the indemnitor’s insurance company to make sure that the indemnitee is properly identified as a named or additional insured.

The whole policy should be reviewed to make sure there are no exclusions that may interfere with the risk transfer



CERTIFICATES OF INSURANCE

- Sole Negligence Exclusion
 - Some additional insured endorsements include the sole negligence exclusion. This exclusion eliminates coverage for claims or suits that result from negligence committed solely by the additional insured (no coverage is provided if the named insured did not contribute to the loss anyway).
 - Some endorsements limit coverage to injury or damage caused, wholly or partly, by acts or omissions of the named insured (policy holder). (Excludes situations where the named insured did not contribute to an accident resulting in a claim against the additional insured).
 - Blanket additional insured (This endorsement fulfills the obligation to name the additional insured when the named insured agrees in written contract to add a person or organization as an additional insured).





WHAT YOU CAN DO BEFORE ACCIDENT

Best practices

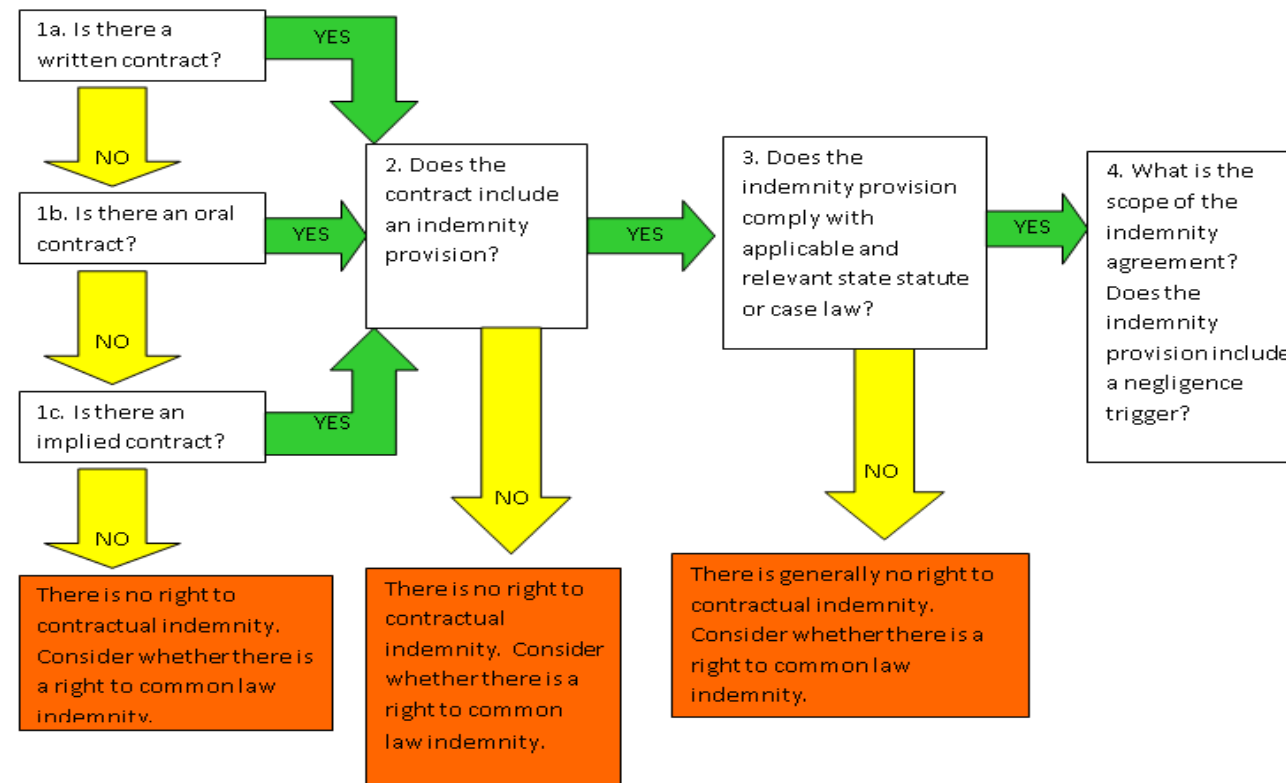
Require all subcontractors to provide a copy of their insurance certificate identifying all appropriate parties as insureds, identifying the appropriate policy limits and require the subcontractors to also provide a copy of the actual policy and its endorsements.



Risk Transfer Best Practices



CONTRACTUAL INDEMNIFICATION





QUESTIONS TO CONSIDER

- Does the jurisdiction allow for indemnification?
- Does the jurisdiction allow for indemnification of sole negligence?
- Does the jurisdiction prohibit indemnification as to any particular group?
- Is “pass through indemnification” permitted?
- What specific language if any is required?
- Is Workers’ Compensation an issue?

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Current Industry Trends Re: Indemnification Clauses

- The current trend for some carriers to take on tenders pre-suit is that they cannot accept the tender because it is not in litigation yet.
- This posturing often leads to unnecessary and expensive litigation for the underlying due to the unresolved risk transfer
- Thus, it is important to see what the coverage and/or indemnification triggers are, as the most common language states: from and against claims, damages, losses, suits...
- While it is possible, it is very rare that the only trigger for an indemnification or insurance clause in a contract is that a suit be filed.

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Basics of Construction Contracts



CONTRACT REVIEW INITIAL STEPS

- Incorporation of Prime Contract (Owner/Contractor Contract)
 - Need to review all contract documents, including any documents incorporated into the contract, as they will dictate the terms and can create additional exposures that are not apparent from the contract.
- Plans and Specifications
 - You should review the plans and specifications prior to starting work and really before signing the contract.



Typical Contract Review Provisions Contain the Following

Scope of Work

- Make sure what was proposed is what is included in the contract

Deadlines and Work Schedules

- Must determine whether schedule is reasonable and can be met. Failure to meet deadlines may be a material breach of the contract resulting in damages.

Design Obligations

- Beware of any design obligations that Contractor attempts to place upon you if you are not doing design work. It can create a professional liability exposure you were not anticipating.

Additional Contract Review Provisions

Pay-if-Paid

The Contractor has no obligation to make any payments to you for work performed unless and until Contractor receives payment from the Owner.



Change Orders

Make sure there is no provision for oral change orders. All change orders shall be written and agreed upon prior to starting the changed work. Further, you should have an agreement on pricing and scheduling changes before any work proceeds.





Additional Contract Review Provisions

Disputed Work

- Be careful of provisions that require you to continue to work through any dispute regardless of whether Contractor makes any payment for the disputed work. Minimally, negotiate that you will be paid some of the disputed costs if required to continue work despite dispute.

Delays

- Make sure that you are not responsible for damages for delays that are beyond your control. Language should be included which allow for an extension of time to complete your work if delay is beyond your control.

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More Typical Contract Review Provisions

Authority to Act on Behalf of Contractor

- Make sure that the Contractor is required to have an authorized representative on-site daily to act on its behalf and authorize any changes needed.

Site Conditions

- These provisions deal with differing site conditions on a project and who bears the risk of unanticipated subsurface or concealed conditions. These provisions obligate you to provide a notice of differing conditions within a specific timeframe and failure to comply can result in you incurring all liability for additional costs incurred.

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Contract Review Provisions

Termination Provisions

- Review closely the conditions that will trigger termination for default. There should be a time for notice and subsequent cure of the default prior to contract termination.
- Remove Contractor subjective standards for termination
- Remove provisions that allow the Contractor to seize possession of your materials, equipment, tools, construction equipment, and machinery to use for completion of the work.
- Review all termination for convenience provisions and your obligations if the contract is terminated for convenience. Make sure, at a minimum, that the Contractor is responsible for payment of all work performed and that payment by Contractor is not a release of any other payments due.

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**Contract
Review
Provisions**

LOSS OR DAMAGE TO COMPLETED WORK

Make sure the Contractor becomes responsible for loss or damage to your work once completed.



LIMITATION OF LIABILITY CLAUSES

Limits a party's liability to a predetermined amount or type of recovery.



DISPUTE RESOLUTION

Determine what types of dispute resolution are acceptable. Most require arbitration.



Contract Review Provisions

ENTIRE AGREEMENT

Make sure that the contract constitutes and supersedes any prior agreements or understandings between the parties.



GUARANTY AGREEMENT

These provisions expose the personal assets of all signatory guarantors to all liability and damages that may be asserted by the Contractor



OCIP or CCIP REQUIREMENTS

Review these documents to ensure adequacy of program. It should be noted that most general liability policies will exclude coverage for work being performed under an OCIP or CCIP.



FINAL CONTRACT REVIEW PROVISIONS



Waiver of Consequential Damages

Negotiate a mutual waiver of consequential damages.

Examples: loss of profits, loss of use, and loss of value.



Lien Waivers

Make sure that lien waivers/releases are conditional upon payment by the Contractor. Lien waivers are valid and enforceable in Colorado Choice of Law Colorado law should apply and govern the terms of the contract. Also, provide for venue where you are located.



Attorney Fees and Costs

Make sure there is a provision that awards attorney's fees and costs to the prevailing party in the event of a litigation, arbitration, or other dispute resolution proceeding. Without such a provision, attorney fees cannot be granted in Colorado.



Contract Review Provisions



Where one party fails to perform as agreed (either in performance or payment)

Breach must be material

The non-breaching party is entitled to a remedy

Most frequent remedy for breach is monetary damages

Other types of damages available: specific performance and injunctive relief

Non-breaching party is compensated by putting it in the same position as if the breach not occurred

Non-breaching party has a duty to mitigate the damages



THANK YOU!

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